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ARGENTINA: The Fight Against Inflation

Argentina is obviously still in the early stages of its fight against hyperinflation, which reached an 800 percent annual rate early this year. The first returns have been favorable.

- The strong popular consensus that was necessary to stop hyperinflation in Europe during the 1920s now exists in Argentina. That consensus did not exist 12 months ago.
- The Argentine government has studied carefully the successful cases of ending hyperinflation in Europe and has formulated an excellent game plan including introduction of a new currency, the austral.
- Taking from these historical examples, Argentine policymakers know that the introduction of a new currency must coincide with elimination of the government deficit.
- They also must know that the deep recession caused by real wage reductions during the freeze period can last less than 12 months--short enough to reasonably hope to hold together the popular anti-inflation consensus.

Indeed, over the past three months, the government in Argentina has apparently spent less than it has taken in, the freeze is working, and the consensus is still holding.

We are seeing some signs that pressure may be building on Alfonsin, however.

- The government's future wage policy and the current status of real wages has been the subject of a growing domestic debate.
- While confirming its commitment to wage and price controls, the government indicated that some private sector wage increases would be allowed in January.
- In addition, "under-the-table" wage increases by employers to avoid unrest and retain skilled labor are occurring with greater frequency,

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-- Consumer prices rose slightly in November on a month-to-month average basis, the first increase in the rate of inflation since the new economic plan was introduced in mid-June. Government figures do not include "under the table" price charges.

A number of factors bear watching over the next few months that could sidetrack Alfonsin's efforts.

- The willingness of labor to accept minimal wage increases will be crucial. The government calculates that purchasing power fell about 5 percent from May to October.
- The depth and length of the recession that results from this income decline. GDP has fallen at an increasing rate over each of the last three quarters; including an estimated 5 percent decline in July-September.
- The manner in which Alfonsin selectively changes prices and wages in early 1986 and the way he is able to police wage and price increases.

While it is possible to be sanguine about the short term prospects for ending hyperinflation in Argentina, i.e., to attain a fairly low level of inflation during a one- to three-year post-freeze expansion, the longer-term prospects are not good.

- Alfonsin has made it clear that the government will not reduce its large role in the economy.
- Labor will, of course, remain a strong force in Argentina.
- It also will be very difficult to improve tax compliance.

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